

United States Postal Regulatory Commission  
901 New York Avenue NW, Suite 200  
Washington, DC 20268-0001  
United States of America

27 August 2012

**Re: Section 407 Inquiry, Docket PI2012-1**

### **CONTRIBUTION FROM NORDIC POSTAL OPERATORS**

This contribution is being submitted jointly by the public postal operators of the five Nordic countries: Denmark, Finland, Iceland, Norway and Sweden. We were very interested to learn of the Postal Regulatory Commission's inquiry regarding rates and classifications for international postal products and services exchanged among postal administrations to be negotiated at the 25<sup>th</sup> Congress of the Universal Postal Union (UPU). We would like to thank the Commission for conducting this inquiry, as we believe it is very important to bring greater transparency and understanding to the topic of international rates (terminal dues) and we hope that the Commission will accept our contribution despite our foreign status.

As non-US entities, we will not comment on relevant US regulation. We would, however, like to comment on the underlying principles governing terminal dues because it appears to us that these principles are relevant for a proper assessment of proposals to be considered at the Doha Congress of the UPU. In addition, these principles and the terminal dues that result, have a substantial and harmful effect on our postal operations.

#### **1. Main characteristics of the proposed UPU-system for rates and classifications for international products (terminal dues)**

Our comments will be limited to the system for rates and classifications for letter post items, i.e. letters and packets with an upper weight limit of 2 kg. ("the terminal dues system").

The Postal Operations Council (POC) of the UPU has proposed a terminal dues system for the upcoming UPU congress that is basically a continuation of the present system. This system groups all UPU countries into 5 main groups and some sub-groups according to their assessed level of development. Our comments will focus upon the system of terminal dues applied to the group of around 23 most industrialized countries, group 1.1, to which both the United States and the five Nordic countries belong.

According to the POC proposal, the rates to be applied for mail exchanges between countries belonging to group 1.1 for the next UPU-cycle (2014-2017) would, at the outset, be based on domestic postage for similar products – 70% of domestic postage for a 20 g letter item and a 175 g large envelope respectively. To the extent that domestic postage is based on costs in group 1.1 countries, this formula produces international rates that are also reasonably cost based, in addition to being reasonably non-discriminatory relative to similar services offered to domestic mailers. However, the UPU terminal dues system for group 1.1 also contains a cap and a floor on the rates. In practice, rates for delivery of international mail in almost all industrialized countries are capped. In this way, the formula that produces reasonably cost-based and non-discriminatory rates is not allowed to function, and the resulting charges for delivery of international mail are substantially below cost for many industrialized countries.

The POC proposal basically continues the present rate regime, including preserving the cap mechanism which has been in place since the 1999 Convention. Preservation of the cap for another four years means, firstly, that those countries that already today receive below cost rates for delivering international mail will continue to be underpaid for their services at least until 2018. As stated above, this concerns most industrialized countries, and for some countries, the amounts involved are substantial. Secondly, keeping a cap without possibilities for adjustment (beyond a prescribed 3% yearly increase) for such a long period as until 2018 means that the system excludes possibilities of adjustments to changing market conditions in a time where the relevant markets change dramatically as letters are being substituted by electronic alternatives and packages are increasingly serving the booming e-commerce business.

Furthermore, the Doha Congress will negotiate and decide the principles guiding the work on the terminal dues system for the period starting in 2018. In the opinion of the Nordic postal operators, it is of vital importance to ensure that these principles lead towards a terminal dues system that is sufficiently flexible and robust to handle the fundamental challenges facing the postal sector going forward.

## **2. Main concerns related to the present and proposed UPU terminal dues system**

The Nordic postal operators have three main concerns related to the present and proposed UPU terminal dues system:

### **2.1. Compatibility with sound regulatory principles and modern competition law**

Increasing competition among public postal operators in the industrialized countries and between public postal operators, on the one hand, and global delivery companies, on the other hand, requires closer attention to the principles of national regulatory and competition rules.

In this regard, Prof. Damien Geradin has prepared a legal opinion at our request on the compatibility of the proposed UPU Terminal Dues Target system with EU law (copy attached). Prof. Geradin is a leading expert<sup>1</sup> on regulatory law of the European Union, also applicable in the European Economic

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<sup>1</sup> Professor at Tilburg University (NL), the College of Europe (BE), and University of Michigan Law School (US);

Area (which includes Iceland and Norway). Although mainly focused on compatibility of the POC terminal dues proposal with EU Law, the opinion also addresses questions about implications on exports from third party countries to the EU based on UPU terminal dues. In brief these are the main conclusions:

- The POC proposed “target system” is not compatible with the EU Postal Directive and EU competition rules because it:
  - Constitutes a prohibited “price-fixing” agreement;
  - Discriminates between domestic and other EU/EEA mailers, discrimination based on origin country; and
  - Results in below cost terminal dues in many Member States.
- Both Designated Operators (public postal operators) and Member States are exposed to possible charges of infringement of EU law.
- Designated Operators of non-EU/EEA countries agreeing to the target system could also be found in violation of EU competition rules as long as their actions have an effect on the EU market.

While we have not studied the compatibility of the proposed UPU Terminal Dues Target system with US law and postal regulation, we believe that the basic policy objectives underlying European postal regulation and competition law may correspond to public policy objectives in the United States as well. Without making any suggestions on the specifics of U.S. law, we hope that the analysis and conclusions described above may constitute a valid contribution to your inquiry in light of our common traditions of free markets, fair competition, and cost-based public services.

## 2.2. Rigidity and inflexibility of the proposed UPU terminal dues system

Rapidly changing market conditions — sharp declines in letters, increasing volumes of e-commerce packets, unforeseeable changes in costs and prices — require more cost-based and flexible remuneration to ensure sustainability of the present postal system. The preservation of the cap regulation for a period as long as up to 2018 presents a major risk of undermining the financing of the international postal network, especially in net importing countries, which include, but are not limited to, the Nordic countries. Furthermore, if the UPU members fail to focus on alternative solutions during the next four year UPU cycle, the rigidity of the system and the risk of underfinancing could be extended even beyond 2018.

The actual and expected growth of relatively heavy items stemming from e-commerce will likely increase the underfinancing from terminal dues, putting the sustainability of the present system at risk. Against this background, the Nordic postal operators highly question the robustness of the present and proposed UPU terminal dues system in meeting the challenges posed by the dramatically changing market conditions going forward.

### 2.3. Fundamental unfairness to mailers and merchants in many countries, including the Nordic countries

As described above, the cap in the UPU terminal dues system produces rates that are lower than rates offered to domestic mailers for similar services and rates that are, in many cases, substantially below direct costs. This scheme creates a hidden subsidy of considerable value that flows from the postal operators and their customers in net importing countries to postal operators that are net exporters of mail. This effect is increased if the net importing country has relatively high costs compared to the net exporting country (as is the case in the Nordic countries generally). At the same time the cap on terminal dues payments among industrialised countries fosters unjustifiable distortion between merchants in sending and receiving countries.

The Nordic countries are very much harmed by these factors because we, in general, are net importing countries with higher costs than many other countries. We recognize, of course, that many postal officials justify their unwillingness to pay terminal dues comparable to our domestic postage by arguing they should not have to pay the relatively high postage rates in countries like the Nordic countries while they have achieved low postage rates in their countries. This reasoning is incorrect and unfounded, however. In all industrialized countries, the main drivers of postal costs are factors such as mail volumes per capita, labour rates, and geographic and climatic conditions. In the economically highly efficient Nordic countries the labour rates are high due to economic factors beyond the control of the postal operators, and the climatic, and in some countries the geographic, challenges are extreme. The Nordics necessarily incur high costs in providing a level of service that is not extravagant even though the service quality is high compared to postal service in most other countries. Our studies have shown that we are operating at a high level of efficiency given the environment in which we operate. As an example, to reduce costs the Nordic postal operators have converted (or are in the process of converting) the vast majority of their post offices to “post-in-shops.” Such cost-savings measures have been extremely difficult for us politically and taken many years to achieve.

Furthermore, the Nordic postal markets are generally characterized by fierce competition from new communication channels. All Nordic operators already have lost and continue to lose extensive letter volume from electronic substitution. Denmark, for instance, has already lost around 45% of letter volumes since 2001. This development in a very competitive environment puts both prices and unit costs under unprecedented pressure.

Any loss incurred on below cost terminal dues rates for imported mail must necessarily be covered by our other customers. In this way, Nordic mailers are de facto subsidizing designated postal operators in low cost net exporting countries. Moreover, it is not at all clear whether outbound international mailers in these net exporting countries really benefit from such a scheme. As the UPU report by Adrenale Corporation<sup>2</sup> makes clear, international postage rates have not historically been closely based on terminal dues. Therefore, low terminal dues do not in themselves lead to low international postage.

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<sup>2</sup> Adrenale Corporation, *Market Research on International Letters and Lightweight Parcels and Express Mail Service Items* (Mar. 2010), pages 29 to 30. This report was prepared for the UPU and may be obtained from [www.upu.int](http://www.upu.int).

Where below cost terminal dues actually are translated into below cost international postage, still wider distortions may result. For example, local merchants may be substantially harmed by below cost postage for imported goods/e-commerce. In recent years, we have seen a rising tide of small packet shipments. The costs incurred in delivering small packets are especially poorly compensated under the present and proposed terminal dues systems for Group 1.1 countries in particular. Therefore, this trend appears likely to worsen with the rise of e-commerce unless immediate and long term corrective measures are taken in the Doha Congress. If no forward steps are taken, these sorts of distortions may harm all industrialized countries, including those where the designated postal operator itself benefits from too low prices in the short term.

### **3. Principles that should guide the development of the Commission's view on rates and classifications established in the 25<sup>th</sup> Congress of the UPU**

We shall not presume to advise the Commission on the legal principles which should be followed with respect to particular issues which it must decide. We are, however, quite familiar with the many important contributions of the Commission to postal regulation from papers presented at postal policy seminars and published articles. The transparency of Commission proceedings and the quality of operational analysis have had a major and beneficial effect on postal regulation worldwide. As such the Commission fulfills a major global role in setting benchmarks for best practices.

From this perspective, therefore, we would like to urge the Commission to analyze carefully and transparently all aspects of the terminal dues system proposed for consideration in the Doha Congress. Such an analysis should preferably not be limited to the terminal dues system for the coming UPU cycle (2014-2017), but also include the principles that should guide the work on the terminal dues system from 2018 and beyond.

In order to provide a better ground for a responsible development of the terminal dues system in the long term, Denmark, supported by several countries including all of the other Nordic countries, has submitted Proposal 81 (attached). Proposal 81 amends Proposal 37, the resolution that will guide the work on the future terminal dues system over the next cycle. Proposal 81 addresses many of the concerns expressed in this paper. It is fair to say that we — Denmark and the other Nordics including our governments as well as the postal operators — received wide support for bringing up our concerns over to the UPU-terminal dues system, in general, and for the proposed amendments to Proposal 37 in particular. This support went far beyond the countries that were able to formally subscribe to the proposal during the short time we had available for seeking support prior to the relevant deadline of 23 July. For these reasons, we believe that a well-reasoned evaluation by the Commission could do much more than provide technical analysis for the U.S. government. It could also have an important and positive influence on the thinking of the wider international postal community.

Although the 25<sup>th</sup> Congress of the Universal Postal Union is imminent, it is our understanding that the proposals now on the table related to the issue that is subject to this inquiry and that will be negotiated in Doha, leave room for various solutions. Some will be better adapted than others to the present situation and the challenges ahead. It is therefore our hope that the Commission will give this important subject the attention and priority it deserves.

Submitting on behalf of the public postal operators in Denmark, Finland, Iceland, Norway and Sweden,

Kristin Bergum  
Vice President, Posten Norge AS

Attachments:

UPU, Doha Congress, Proposal 81 (amending Proposal 37).

Prof. Damien Geradin, "Legal Opinion on the Compatibility of the Proposed Target System for Terminal Dues with EU Law", 29 April 2012.